

**Bills Committee on Securities and Futures and Companies Legislation  
(Uncertificated Securities Market Amendment) Bill 2014 (“Bills Committee”)**

**Responses from the Administration and the Securities and Futures Commission (“SFC”) to  
comments given by deputations to the Bills Committee**

| Comments  | The Administration’s and SFC’s responses  |
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| <p><b>Mode and Timeframe of Implementation</b></p> <p><i>Organisations: The Hong Kong Association of Banks (“HKAB”), Consumer Council (“CC”), Hong Kong Securities Association, Hong Kong Exchanges and Clearing Limited (“HKEx”), CLP Holdings Limited (“CLP”) and Federation of Share Registrars Limited (“FSR”)</i></p>  |   |
| <p>1. Hong Kong should aim for a mandatory uncertificated securities market regime. In light of this,</p> <p>(a) the option for securities to be transferred from uncertificated to certificated form should be removed;</p> <p>(b) a transitional period should be in place to allow sufficient time for investors to adapt to the changes though a dual system approach would add complexity to the system development efforts required and the subsequent market operations involved;</p> <p>(c) when the market is ready, there should be a cut-off time after which it is not an option for prescribed securities to be held in certificated form; and</p> | <p>We agree that once the market is ready, the uncertificated securities market regime should be implemented fully and the option of rematerialization (i.e. from uncertificated form into certificated form) should be removed. Meanwhile, the interim measure of having a dual system will facilitate the gradual implementation of the uncertificated securities market. We also agree to consider measures to encourage the use of uncertificated securities, including mandating paperless IPOs and launching investor education programmes.</p> |

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| (d) measures to encourage the use of uncertificated securities, in preference to certificated securities, should be adopted in the market (e.g. investor education programmes and requiring initial public offerings ("IPOs") applications to be conducted in uncertificated form).   |  |
| 2. In terms of good corporate governance, there should be equality of treatment of all shareholders – whether with or without scrip. Proper checks and balances should also be established with respect to the functions of the registrar and the clearing house for investor protection. Legislative safeguard is therefore welcome.   | Noted and agreed.  |
| 3. It may take at least 18 to 24 months for the development of a new information technology ("IT") system to cater for the uncertificated securities market. Accordingly, the earliest time to launch the uncertificated securities market may be around 2017-18. In addition, other market intermediaries/stakeholders, including stockbrokers and banks, may also need considerable time to rebuild and/or upgrade their information technology systems. The time gap between the passing of the Bill and the launch of the uncertificated securities market could be at least 36 months or more. | <p>The preparation for the uncertificated securities regime includes the following main tasks –</p> <ul style="list-style-type: none"> <li>(a) legislative process for amending the primary legislation;</li> <li>(b) market consultation on and making of the subsidiary legislation;</li> <li>(c) finalization of operational model and technical specifications of the IT infrastructure; and</li> <li>(d) system enhancement and testing.</li> </ul> <p>We will continue to work closely with market participants and stakeholders to deal with the above issues with a view to implementing the new</p> |

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|  | regime as soon as possible.  |
| <b>Operational Model and Rules (i.e. Subsidiary Legislation to be made by SFC)</b><br><br><i>Organisations: FSR, HKAB and the Law Society of Hong Kong ("LS")</i>  |  |
| 4. It is uncertain when the detailed work flows and the exact operational model will be finalized, in particular in respect of certain corporate action issues and the role of the Central Clearing and Settlement System, thus affecting the preparation of the Rules and the launch time of the uncertificated securities market regime. | SFC will continue the discussion with HKEx and FSR on the technical details of the operational model (including those relating to the provision of corporate action services) with a view to reaching consensus as soon as possible.                     |
| 5. Market participants should be given adequate opportunity to review and comment on the Rules before implementation. The relevant operational and technical details should be released as early as possible for conducting consultation with stakeholders.  | SFC is working with HKEx and FSR on the operational and technical details. SFC plans to conduct market consultation on the draft Rules in 2015. Ample time will be given for stakeholders to consider and comment on the draft Rules.                    |
| <b>Fees and Charges</b><br><br><i>Organisations: FSR, HKAB, CC, CLP, the Hong Kong Institute of Chartered Secretaries ("HKICS") and the Lion Rock Institute</i>  |  |
| 6. Under the uncertificated securities market regime, certain fees and charges can be streamlined and reduced as a result of improved operational efficiency and reduced cost.   | We are mindful that the issue of fees is of concern to all stakeholders. The guiding principles with respect to fees under the uncertificated securities market regime are that fees should be reasonable (for all parties concerned), commensurate with |

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|  | services provided, conducive to encouraging innovation and market development, and should not offset the longer term benefits of an uncertificated securities market environment.  |
| 7. The potential increased costs of share registration services as a result of the requirement to keep two sets of registers relating to certificated and uncertificated securities should not be pushed down to listed issuers only but should be spread amongst investors in accordance with the "user pays" principle.  | For share registrars, the services provided and fees charged will be under a competitive environment.  |
| 8. Under the current paper-based system, investors who opt to hold their securities in paper form are able to collect dividends from the issuer directly (either by cheque or autopay into their account) without paying any fee. Under the uncertificated securities market regime, will investors still have such a choice or will they have to pay a dividend collection fee to a bank or broker? | Under the uncertificated securities market regime, there will be different account types. Not all account types will be provided by banks or brokers, and hence investors will not be obliged to keep their uncertificated securities with such entities. Investors will be able to choose which account type to place their uncertificated securities in, taking into account their own needs as well as the fees and services associated with different account types. |
| <p><b>Increase in number of registered shareholders</b></p> <p><i>Organisation: HKICS</i></p>  |  |
| 9. Under the uncertificated securities market regime, the number of registered members will significantly increase. This will  | Under sections 831 and 833 of the Companies Ordinance (Cap. 622) ("CO"), subject to certain  |

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| <p>increase the quantities of printed corporate communications, dividend cheques and advices to be sent to shareholders by post, and pose logistical challenges for shareholders' meetings such as locating suitable conference venues. These will result in additional costs to listed issuers. In order to resolve such problems, consideration should be given to mandating shareholders holding shares in uncertificated form to –</p> <ul style="list-style-type: none"> <li>(a) provide email addresses for recording in the members register (uncertificated shares);</li> <li>(b) be deemed to have given consent to receiving corporate communications by electronic means;</li> <li>(c) receive their dividends via autopay to a bank account (for shareholders holding bank accounts in Hong Kong);</li> <li>(d) receive their dividend advices by electronic means;</li> <li>(e) complete and send proxy forms for voting at shareholders' meetings by electronic means; and</li> <li>(f) exercise voting rights via online voting facilities.</li> </ul> | <p>conditions (including consent given by a member), a company incorporated under the CO or its predecessors may send or supply a document to a member in electronic form or by making it available on a website. The requirement for the recipient's consent, which is also adopted in other jurisdictions such as the UK and Australia, is considered necessary because electronic communications may not suit everyone, in particular, those recipients who may not have access or easy access to IT facilities.</p> <p>Under the uncertificated securities market regime, those shareholders who opt for shares in uncertificated form may likely have e-mail addresses and ready access to IT facilities. The SFC will explore how electronic communications between participating companies and those members who opt for uncertificated shares can be encouraged.</p> <p>Regarding the payment of dividends, the CO does not specify how dividends may be paid to the members. Currently, investors are able to receive their dividends by autopay. This option will continue under the uncertificated securities market environment.</p> |

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| <p><b>Register of members</b></p> <p><i>Organisations: LS, CC and HKICS</i></p>   |   |
| <p>10. In respect of the register of members, the Rules should be clear about the following –</p> <p>(a) how the two parts of the register will be maintained and in the event of inconsistency which part of the register will prevail; and</p> <p>(b) a member will retain legal title until the new entry is made in the relevant part of the register.</p> <p>A mechanism should be in place to ensure accuracy in the record details of holdings in the two parts of the register.</p> | <p>Details as to how the two parts of a participating company's register of members are to be maintained (including where the register should be kept, what information should be entered into the register and made available for inspection, etc) and how inconsistencies are to be dealt with will be included in the Rules. SFC will consult the market on the draft Rules.</p> <p>The Rules will also include provisions to deal with ensuring the accuracy of the two parts of the register (e.g. provisions requiring that precautions be taken to guard against falsification).</p> |
| <p>11. In accordance with the Company Records (Inspection and Provision of Copies) Regulation (Cap. 622I), the public may inspect the information on the register of members of listed companies, including the shareholders' names, residential addresses and numbers of shares held. This may cause concern to certain investors who would like to maintain their privacy, in particular their residential addresses.</p>   | <p>The inspection arrangements for the register of members prescribed by Cap. 622I will not apply to a participating company. The right to inspect the register of members of a participating company will be governed by the Rules. The SFC will consult the market on the draft Rules in 2015.</p>  |

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| <p><b>Impact on Companies Ordinance</b></p> <p><i>Organisations: LS and HKICS</i></p>   |  |
| <p>12. There are provisions in the CO subsidiary legislation which relate to the transfer of title to shares or the holding of shares in certificated form only and the Bill has not addressed these provisions. Examples include transfer of shares (in paragraph 80 of schedule 1 to the Companies (Model Articles) Notice (Cap. 622H)) and the issue of share certificates upon issue of shares (in paragraph 64 of the Model Articles).</p> | <p>The provisions in the Model Articles are optional for companies. A company should incorporate provisions in its articles that it deems appropriate. In any event, new sections 101AAD to 101AAF provide for the overriding of a company's articles where these conflict with the evidencing and transfer of title to shares in accordance with the Rules.</p>   |
| <p>13. Under the proposed new section 158A of the CO, the traditional timeframes of 28 days and 2 months were referred to in relation to certain procedural matters. It may be necessary to develop a speedy and cost effective mechanism to resolve disputes in a timely manner, for example through a panel mechanism prior to any recourse to the Court system.</p>  | <p>The "traditional timeframes of 28 days and 2 months" under section 158 of the CO to register a transmission of shares allow sufficient time for a company to verify the legitimacy of a request to register a transmission of shares e.g. to examine the relevant probate or court documents. The checks and balances necessary to verify the legitimacy of a request for registration under section 158 will likewise be required under the proposed new section 158A for the uncertificated securities market regime.</p> <p>As regards dispute resolution, this is a general issue and not unique to the uncertificated securities regime.</p> |

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| <p><b>Stamp Duty</b></p> <p><i>Organisations: HKAB, CC and HKICS</i></p>  |  |
| <p>14. The proposed new stamping arrangement for transfers of uncertificated securities and the proposed exemption of the \$5 fixed rate stamp duty for transfer of participating shares without an instrument of transfer are supported. There should be practical guidance for market participants in plain language, together with appropriate “frequently asked questions”, to facilitate compliance with the new stamping arrangement.</p>   | <p>The Inland Revenue Department (“IRD”) will issue a Stamp Office Interpretation and Practice Note to elaborate on the proposed stamping arrangement for transfers of uncertificated securities and the related compliance issues, and upload the relevant information onto the IRD website.</p>  |
| <p>15. There may be a need for special arrangements for stamp duty adjudication, payment and refund in respect of the transfer of shares in uncertificated form under the following circumstances –</p> <ul style="list-style-type: none"> <li>(a) transfer from trustee to beneficial shareholder;</li> <li>(b) transfer from beneficial shareholder to trustee; and</li> <li>(c) stamp duty relief for intra group transfer of shares under section 45 of the Stamp Duty Ordinance (Cap. 117) (“SDO”).</li> </ul> | <p>The three specified scenarios are off-Exchange transfers. Under the proposed stamping arrangement, the authorized participants of uncertificated securities market system who are also regulated entities (which will include brokers, custodians and share registrars) will be able to effect share transfers between trustees and beneficiaries (i.e. (a) and (b)) after making declarations electronically (via the uncertificated securities market system) that the transfers are not subject to ad valorem stamp duty. IRD will then carry out audit checks on these claims. As regards share transfers involving intra-group relief application (i.e. (c)), section 45(3) of the SDO provides that the relevant contract notes or instruments of transfer will not be duly stamped unless they have been adjudicated in accordance</p> |



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|  | with section 13 of the SDO. In this regard, the relevant instruments in paper will be required to be submitted to IRD for adjudication. After having lodged the intra-group relief claims with IRD, the share transfers can be effected by the relevant uncertificated securities market system participants after making a declaration electronically (via the uncertificated securities market system) that the transfers are not subject to ad valorem stamp duty. |
| <b>Implications for H shares</b><br><br><i>Organisation: HKICS</i>   |   |
| 16. Individual shareholders of H shares are expected to opt for holding securities in uncertificated form rather than in the name of nominees so that they will receive their H share dividends in full potentially without the 10% enterprise income tax deduction in Mainland China. | Individual shareholders will have the option to hold their shares in their own names or in the name of a nominee.   |
| <b>Technical comments on individual provisions of the Bill</b><br><br><i>Organisations: LS, HKEx and the Hong Kong Bar Association</i>   |   |
| 17. LS proposed some amendments to sections 2(1), 2(3A), 143B, 159(1) and 626(A) of the CO.  | From the law drafting point of view, we do not consider it necessary to make the suggested amendments. If necessary, we may explain the details during clause-by-clause examination of the  |

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|   | Bill.  |
| <p>18. The Hong Kong Bar Association has commented that –</p> <ul style="list-style-type: none"> <li>(a) a definition for the term “OTC derivative products” should be added since it is referred to in sections 42 and 71 but not defined in either the SFO or the Bill;</li> <li>(b) section 76(1A)(a) should refer to “recognized clearing house” rather than “clearing house” for consistency with section 76 of the SFO; and</li> <li>(c) the reference to “section 158A(2)(a)” in section 159(2)(b) of the CO should be amended to 158A(5)(a) since the former does not refer to any refusal to give notice.</li> </ul> | <p>On (a), a definition for “OTC derivative product” was introduced by the Securities and Futures (Amendment) Ordinance 2014 (6 of 2014) – see sections 52(3) and (4) of that Ordinance. The provision is expected to come into effect in early 2015 and so well in advance of the Bill.</p> <p>On (b), as the chapeau to section 76(1A) refers to “the recognized clearing house”, it is clear from the context that the reference to “the clearing house” in section 76(1A)(a) refers to the same entity.</p> <p>On (c), the wording “described in section 158(2A)(a)” in the proposed new section 159(2)(b) is to qualify “notice”, not “refusal”. It is therefore correct to refer to the new section 158A(2)(a) (instead of new section 158A(5)(a)) in the new section 159(2)(b).</p> |
| <p>19. HKEx proposed some amendments to a number of sections of the SFO, CO and SDO.</p>  | <p>We are discussing these proposed amendments with HKEx with a view to better understanding their concerns.</p>   |

Financial Services and the Treasury Bureau  
Securities and Futures Commission  
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